GENERATE

Journal of Banks and Financial Institutions

e-ISSN: 3089-9761

Vol 01 (2) 2025 p. 116-127

Corresponding author:
Aoktavia Taniatul Romadhani
Email: aoktaviatania@gmail.com

Received 23 September 2025;
Accepted 2 October 2025;
Published 4 October 2025.

Conflict of interest statement:
The author (s) reported no conflict of interest

DOI: http://doi.org/10.70764/gdpu-jbfi.2025.1(2)-10

A QUALITATIVE STUDY OF MSMEs PERCEPTION AND PRACTICES TOWARDS ISLAMIC FINANCE IN RURAL AREAS

Aoktavia Taniatul Romadhani[1]

[1]Politeknik Negeri Semarang, Indonesia

ABSTRACT

Objective: This study aims to explore the perceptions and practices of micro, small, and medium enterprises (MSMEs) in rural areas regarding Islamic finance, highlighting the gap between ideal perceptions and actual practices.

Research Design & Methods: A qualitative phenomenological approach was used to capture the lived experiences of MSME actors MSMEs in adopting Islamic finance. Data was collected through in-depth interviews and thematic analysis was used to identify patterns and challenges..

Findings: The findings reveal significant differences between positive perceptions of Islamic finance and its practical implementation. Although most respondents expressed strong support for Sharia principles—valuing fairness, interest-free systems, and alignment with religious values – its implementation is hindered by limited access to Islamic financial institutions, complex administrative procedures, and a lack of knowledge about available Shariah-based financial products. The study also highlights the potential of Islamic fintech and government support as key drivers for overcoming these barriers.

Implications & Recommendations: This study shows that improving financial literacy, simplifying administrative processes, expanding access to Islamic financial services in rural areas, and utilizing fintech innovations can significantly increase MSME participation in Islamic finance. Stronger policy support and targeted programs for rural MSMEs are recommended to strengthen the Islamic financial ecosystem.

Contribution & Value Added: This study contributes to the literature by providing empirical insights into the perception-practice gap among rural SMEs in adopting Islamic finance. It highlights the interplay between religious values, structural constraints, and technological opportunities, and offers practical recommendations for policymakers, financial institutions, and technology providers to promote inclusive Islamic finance.

Keywords: Islamic Finance, MSMEs, Rural Development

JEL codes: G21, O16, P34
Article type: research paper

INTRODUCTION

Islamic finance is gaining widespread attention in various countries, including small and medium enterprise (SME) development in rural areas. SMEs are not only seen as drivers of local economic growth but also as strategic tools for improving the well-being of rural communities. By applying the principles of Islamic finance, which emphasize justice, transparency, and sustainability, rural SMEs can access more inclusive financing that aligns with Sharia values. This ultimately encourages the creation of new jobs, strengthens local economic independence, and contributes to more sustainable poverty alleviation (Manzoor et al., 2021).

Micro, Small, and Medium Enterprises (MSMEs) are often referred to as the backbone of Indonesia's economy due to their dominant contribution to supporting national growth. Based on empirical data, this sector contributes more than 60% to the Gross Domestic Product (GDP). It absorbs over 90% of the workforce across various sectors, making it the primary driver of a people-centered economy (Salsabillah et al., 2023). The strategic role of SMEs is not limited to job creation but also includes strengthening the local economic structure through income distribution, poverty alleviation, and enhancing social resilience. With its broad base and presence spanning nearly every corner of the country, SMEs also serve as a crucial instrument in maintaining economic stability, expanding public access to business opportunities, and sustainably reinforcing regional economic self-reliance.

The recent statistics from the Ministry of Cooperatives and Small and Medium Enterprises show that the number of micro, small, and medium enterprises (MSMEs) in Indonesia has significantly increased, reaching approximately 66.2 million units by 2023. Of this total, more than a quarter, or around 25.5%, have utilized sharia-based financial services, which shows a considerable increase compared to 2019, when the percentage was only around 17%. This development not only reflects the growth in the number of MSMEs but also indicates an increase in the level of awareness and trust of business actors in the sharia financial system, which is considered fairer, transparent, and in line with sustainability principles. This increase in adoption is closely linked to various initiatives by the government and financial industry players who have actively expanded access and provided a more diverse range of sharia financing instruments, further strengthening sharia financial inclusion in the SME sector.

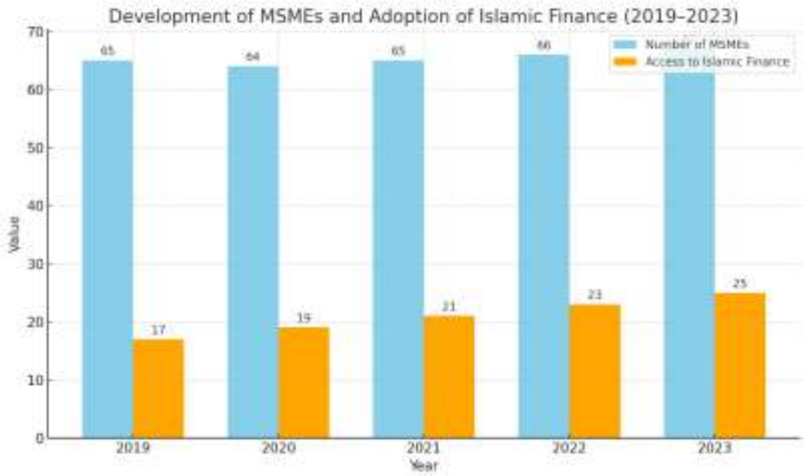

Figure 1. Development of MSMEs and Adoption of Islamic Finance (2019-2023)

Many studies confirm that SMEs in rural areas have the potential to reap significant benefits from the implementation of financing schemes based on sharia principles, especially when SME owners and managers have adequate knowledge of Islamic finance. The study by Balushi et al., (2019) indicates that factors such as Islamic financial literacy and the personal characteristics of SME owners and managers play a significant role in influencing their decision to adopt Islamic financing, while internal company characteristics have relatively less influence. Additionally, innovative financing models, such as Sharia-based crowdfunding, are beginning to gain attention as alternatives that not only comply with Islamic law but also provide creative mechanisms to support the sustainability and growth of SMEs, especially amid the demand for compliance with Sharia principles in the modern business ecosystem (Abdeldayem & Aldulaimi, 2023). In this context, enhancing Islamic financial literacy and strengthening marketing strategies for Islamic financial products are crucial for expanding awareness, fostering trust, and increasing the participation of rural SMEs in utilizing Islamic financial services (Balushi et al., 2019).

The study of SME perceptions and practices regarding Islamic finance in rural areas is highly urgent, especially given the lack of empirical research that comprehensively highlights this phenomenon. Most previous studies have tended to focus on urban contexts or have only used quantitative approaches, thereby failing to fully capture the dynamics, nuances, and complexity of the experiences of SMEs at the grassroots level. Therefore, a qualitative approach is relevant and necessary to delve deeper into the social, cultural, and economic factors shaping SMEs' perceptions of Islamic finance, understand how they interpret and apply Sharia principles in their daily business practices, and identify both structural barriers and opportunities that arise in the process of accessing and utilizing Sharia-based financial services in rural areas.

A comprehensive understanding of rural MSMEs' perceptions and practices regarding Islamic finance is essential in formulating more targeted and effective sharia financial inclusion strategies. This study's findings are expected to provide valuable input for policymakers, practitioners in Islamic financial institutions, and academics in developing programs and financial products that align with the needs and characteristics of rural SMEs. Furthermore, this research is also expected to enrich the theoretical body of knowledge in the literature related to Islamic finance, SMEs, and efforts to empower the rural economy.

Thus, this study specifically aims to explore the perceptions and practices of micro, small, and medium enterprises (MSMEs) in rural areas regarding the implementation of Islamic finance. This research focuses on identifying the gap between normative understanding of the ideal principles of Islamic finance and the reality of its implementation at the practical level. This approach is expected to contribute to the academic literature on the dynamics of acceptance and implementation of Islamic finance in rural communities, while also offering an empirical basis that can be used to formulate policies and mentoring strategies that are more adaptive, effective, and tailored to the needs of MSMEs in rural areas.

LITERATURE REVIEW

The Concept of Sharia Finance

Islamic finance, better known as sharia finance, is a financial system based on Islamic law (sharia) principles to achieve justice, sustainability, and balance in economic activities. This system is based on the prohibition of usury or interest, which is considered harmful, gharar or excessive uncertainty, maysir or harmful speculation, and the prohibition of investment in sectors that are not in line with Islamic values, such as the alcohol industry and gambling (Ayub, 2007). Instead, Islamic finance emphasizes the application of profit and loss sharing (PLS) principles, the existence of tangible assets as the basis for transactions (asset backing), and fairness in every contract, so that financial transactions are not only profit-oriented but also focused on blessings, transparency, and social benefits. With these characteristics, Islamic finance is seen as capable of becoming an alternative financial system that is more inclusive and ethical, and increasingly relevant in the modern era because it prioritizes moral and social responsibility in economic activities.

According to Antonio (2001), the Islamic financial system has several fundamental characteristics that distinguish it from the conventional one. (1) All activities must be free from riba or interest, which are considered harmful and unfair, (2) Islamic finance also avoids practices of gharar (excessive uncertainty) and maysir (speculation or gambling), which have the potential to cause instability, (3) financial transaction mechanisms are based on the principle of profit sharing, so that risks and profits are borne proportionally by the parties involved, (4) every transaction must be based on tangible assets, which emphasizes the connection between Islamic finance and honest and productive economic activities, (5) this system strictly prohibits the financing of activities that are prohibited in Islam, such as the alcohol industry, gambling, or businesses that are harmful to society. These characteristics distinguish the Islamic financial system from the conventional financial system.

Instruments in Islamic finance operate through various contracts designed in accordance with Sharia principles, such as mudharabah, which is a profit-sharing partnership between capital owners and business managers; musyarakah, which is a capital collaboration between parties to run a joint business; murabahah, which is a sale and purchase scheme with an agreed profit margin; and ijarah, which is a lease agreement. Islamic finance is not solely focused on achieving financial gains; it emphasizes broader objectives, such as fostering social sustainability, ethics, and justice in every transaction. These principles make Islamic finance a more stable alternative than conventional financial systems, as it rejects excessive speculative practices and promotes inclusion, social equality, and sustainable development. Several studies also confirm that this approach can make a tangible contribution to strengthening the global financial system's stability while integrating moral values and social responsibility into economic activities (Maksum et al., 2020; Mengistu & Panizzolo, 2023).

Micro, Small, and Medium Enterprises (MSMEs)

Micro, Small, and Medium Enterprises (MSMEs) are widely recognized as a fundamental pillar of the economy, especially in developing countries, due to their crucial role in driving economic growth, expanding employment opportunities, and improving equitable welfare for the community. In Indonesia, MSMEs not only serve as the primary providers of employment but also act as the driving force maintaining the resilience and stability of the national economy, especially during crises or economic slowdowns. Their existence can support the needs of the community from the local to the national level through their high flexibility and adaptability, as well as their tangible contribution to building the economic independence of the people. With a number that is very dominant compared to large businesses, MSMEs have become an essential foundation in creating an inclusive and sustainable economic structure (Maksum et al., 2020; Mengistu & Panizzolo, 2023).

The micro, small, and medium enterprise sector is often seen as the engine of growth that plays a strategic role in driving economic development, creating jobs, reducing poverty, and promoting industrial growth and exports (Nath, 2024). Similarly, Raspati and Kadiyono (2023) emphasize that this sector is not only the economy's main driver but also serves as a vehicle for social empowerment, particularly for women. This is evident from the dominance of micro-scale businesses, which are managed by women and have significantly contributed to national economic recovery following the crisis. Thus, the role played is not limited to the financial sphere but also extends to the social sphere, influencing the strengthening of inclusivity and the resilience of the nation's economy.

Akpan et al., (2021), say that as a strategic platform, MSMEs play a key role in introducing and developing local creative products that reflect the region's potential, identity, and wisdom. Not only does this sector serve as a means of promoting and distributing local products, but it also drives the creation of new business opportunities that can increase per capita income and expand the regional economic base. Furthermore, MSMEs have great potential for innovation and leveraging technological advancements, such as through digital marketing, e-commerce, and social media utilization, to expand product reach to broader markets nationally and internationally. Using technology strengthens local products' competitiveness in the global marketplace and fosters a more self-reliant, inclusive, and sustainable regional economic ecosystem.

The micro, small, and medium enterprise (MSME) sector has proven to have a high level of resilience, especially during the COVID-19 pandemic, requiring business actors to adapt to an uncertain economic situation. In this context, MSMEs have implemented various strategies to sustain their operations, ranging from product innovation and digital marketing to leveraging e-commerce platforms aligned with the advancements of the 4.0 Industrial Revolution era. These efforts aim to boost revenue amid the crisis and form part of a broader business transformation toward greater adaptability and competitiveness (Sularsih & Nasir, 2021).

Socio-Economic Characteristics of Rural Communities

Rural communities generally have characteristics that differ from those of urban communities. Rural communities' economic and social structure is closely related to the availability of basic infrastructure, the quality of education, and support in the form of social assistance programs from the government and associated institutions. Recent research indicates that interventions through financial social assistance, whether through direct cash transfers or specific subsidies, strategically reduce poverty rates in rural areas (Zreik & Haron, 2025). These programs not only help meet the basic needs of households but also contribute to strengthening family economic resilience, improving access to health and education services, and creating opportunities for communities to become more economically independent.

The socio-economic characteristics of rural communities are generally marked by the dominance of the agricultural sector as the primary source of livelihood, with relatively low levels of education and limited access to modern infrastructure (Swain & Ranganathan, 2021). This situation makes rural communities highly dependent on local natural resources, while the diversification of economic activities remains limited. This situation also results in higher poverty rates and more pronounced economic disparities than urban communities, due to barriers in accessing adequate public services, capital, and employment opportunities in broader markets. However, despite these limitations, rural communities possess substantial social capital through solidarity, mutual aid, and social networks rooted in traditional values (Perez-Trujillo & Lacalle-Calderon, 2020). Such social capital plays a crucial role in strengthening rural communities' resilience and adaptive capacity in facing economic, social, and environmental challenges, while also serving as a potential foundation for inclusive and sustainable development in rural areas.

Related to socio-economic development indicators for rural households, the aim is to produce a more comprehensive measurement framework capable of representing the reality of rural community life. This framework typically focuses on economic dimensions, such as household income levels, diversity and stability of employment sources, and social aspects such as access to basic services, including education, health, and the availability of adequate public infrastructure. Additionally, asset ownership, productive assets such as agricultural land and livestock, and non-productive assets such as housing and valuable goods, also serve as important indicators in assessing well-being. The combination of these factors provides a more comprehensive picture of the quality of life in rural communities, while also serving as a reference for identifying socio-economic disparities and formulating more targeted development policies (Panakaje et al., 2025).

The Theory of Planned Behavior in the Context of Islamic Finance

The Theory of Planned Behavior (TPB) provides a significant framework for understanding individual decision-making processes in Islamic finance. Introduced by Ajzen (1991), this theory is widely used to explain the factors that drive individuals' intentions and behaviors in adopting Islamic finance. This theory asserts that the intention to behave is formed from three main aspects: attitude toward behavior, subjective norms, and perceived behavioral control. In Islamic finance, a person's attitude is generally influenced by their belief in Sharia financial products' economic benefits and spiritual values. Subjective norms, such as family, peers, religious leaders, and the community, reflect how much the social environment influences individual choices. Meanwhile, perceived behavioral control relates to individuals' views on the ease, availability of facilities, and accessibility of Islamic financial services or products, ultimately determining the extent to which they feel capable of adopting them.

In Islamic banking, several studies have utilized the Theory of Planned Behavior (TPB) framework to explain why individuals are more likely to use services offered by Islamic financial institutions than conventional banks. Findings from empirical studies, such as those conducted by Pitchay et al., (2019), show that factors such as attitudes toward Islamic products, social norms that create environmental pressure or support, and individuals' perceptions of the ease and ability to use these services have a significant influence on a person's intention to become a customer of Islamic banking. Overall, these components of TPB not only provide a comprehensive picture of the determinants of adoption behavior but also confirm that the main appeal of Islamic banking lies in its ethical framework, fairness, and profit-sharing mechanisms that are in line with Islamic values, thereby strengthening public trust and loyalty to the Islamic financial system.

The Theory of Planned Behavior (TPB) plays a very significant role in explaining individual behavioral intentions in the context of Islamic finance, as it not only highlights religious motivational aspects but also accommodates rational considerations such as economic benefits, ethical principles, and the value of Sharia compliance, which form the basis for adopting these financial services. Although the classical TPB model provides a strong conceptual foundation, many studies emphasize that adding more specific contextual variables—such as levels of Islamic financial literacy, trust in institutions, or product innovation—can strengthen the predictive power of this theory in explaining consumer behavior. Thus, the TPB remains a relevant and adaptive theoretical framework that not only helps understand the factors influencing adoption but also contributes to formulating marketing strategies, product development, and public education to ensure Islamic financial services are increasingly accepted and positioned as an ethical, sustainable, and Sharia-compliant financial solution.

METHODS

This study uses a qualitative approach with a phenomenological study type, which focuses on understanding and exploring the subjective experiences of MSME actors in managing sharia-based finance. Through this approach, the researcher seeks to capture the perspectives, interpretations, and realities directly experienced by the research subjects, thereby understanding how Sharia values are internalized in daily financial practices. Phenomenology is considered relevant because it can reveal the essence of individual experiences that are not only rational but also influenced by spiritual, social, and cultural aspects that surround the lives of MSME actors.

In this study, researchers acted as the primary instruments (human instruments) key to the entire data collection process, supported by in-depth interview guides systematically designed based on innovation adoption theory indicators and Islamic finance principles. The guide contains open-ended questions aimed at exploring the perceptions of MSME actors regarding sharia values, their experiences in using sharia financial products, and the social and spiritual factors that influence their financial management practices. Data collection techniques were carried out through in-depth interviews that allowed for a more personal exploration of meaning and limited participatory observation to capture the real context in the field. Additionally, supporting documents, such as business financial records, Islamic financial service brochures, and documentation of SME actors' activities, were analyzed as secondary data to enrich and validate the research findings. All interviews were recorded with the informants' consent and then transcribed verbatim to ensure the data remained authentic and could be comprehensively analyzed in the analysis phase.

RESULT

Characteristics of Informants

Based on the interviews with 15 informants, it was found that MSME actors in rural areas have quite diverse demographic and business characteristics, including differences in age, education level, type of business, and length of time in business. The results also showed that most MSMEs in rural areas have characteristics that distinguish them from those in urban areas, both in terms of family involvement in the business and the dominance of the trade and food production sectors, which are oriented towards food. The research also revealed that most rural SMEs have distinctive characteristics that set them apart from urban SMEs, including family involvement in the business, a dominance of the trade and food production sectors focused on meeting daily community needs, and limited access to modern infrastructure and financial services. This uniqueness makes rural SMEs economic actors and an integral part of the social system, closely tied to the values of cooperation and local wisdom.

Table 1. Informant Characteristics

Characteristics	Category
Gender	Male (9 people) Female (6 people)
Age	Average 42 years old (range: 28-58 years old)
Education	Elementary School (20%) Junior High School (20%) Senior/Vocational High School (47%) Diploma/Bachelor′s Degree (13%)
Type of Business	Trade (53%) Food production (27%) Services (20%)
Length of Business	Average 8 years (range: 2-20 years)

The characteristics of the informants show a diversity of backgrounds that provide a comprehensive picture of the actual conditions of MSME actors in rural areas. The balanced gender composition shows that men and women play important roles in local economic activities. The wide age range, with an average age in the productive age group, indicates that most business actors are in a phase of life that is mature in terms of experience while still economically active. The varying levels of education indicate differences in knowledge and understanding, which may influence their views on Islamic finance and strategies for managing their businesses. In terms of business type, the dominance of the trade and food production sectors indicates that economic activities in rural areas are still closely related to meeting the community's daily needs, while also having the potential to grow because they are directly related to household consumption. The relatively long duration of business operations, with an average of eight years, reflects the resilience and adaptability of SME actors to market dynamics and economic challenges. This demonstrates that the informants' experiences can provide valuable insight into their perceptions and practices regarding Islamic finance.

MSMEs' Perceptions of Islamic Finance

The analysis's results reveal that informants' understanding of Islamic finance can be grouped into three main categories, reflecting their level of knowledge, experience, and how they interpret sharia principles in their daily business practices.

a. Basic Understanding of Islamic Finance (60% of Informants)

Most SME actors understand Islamic finance simply as a system that avoids usury and is in accordance with Islamic teachings, so they equate it with "interest-free" practices. For example, one informant stated, "Islamic finance does not use interest, in accordance with our religion. But yes, I don't know the details yet" (informant who is a grocery trader). This understanding shows that their perception is still limited to the prohibition of interest. In contrast, other aspects that are the basic principles of Islamic finance, such as the profit-sharing system, various types of contracts, and the prohibition of gharar practices, are not widely known and deeply understood.

b. Intermediate Understanding (Islamic Finance is Considered Fairer (27% of Informants)

Some informants demonstrated a broader understanding of sharia principles, not limited to the prohibition of usury, but also the concepts of profit sharing and contracts in Islamic finance. One informant said, "I know there is mudharabah, murabahah. The point is cooperation, not just avoiding usury but also being fair in sharing risks" (chip producer informant). This understanding aligns with the experiences of some respondents who have interacted with Islamic financial institutions, where they consider the profit-sharing system to be lighter than conventional loan interest rates, as the mechanism adjusts to the conditions and results of the business being run.

c. Deep Understanding (Religiousness Influences Perception (13% of Informants)

Some informants have comprehensive knowledge of various Islamic financial instruments and principles, so they understand the prohibition of usury and recognize the values contained in the system. MSME actors with higher levels of religiosity tend to show a more positive attitude toward Islamic financial services and even consider their use a moral obligation. Most informants (13%) also consider Islamic finance to align with the values in rural communities, such as cooperation and helping one another. This is reflected in the statement of one informant, "In this village, the values of cooperation and helping one another are still strong. Sharia finance is in line with our values" (an informant who is a farmer).

MSMEs Practices in Islamic Finance

Use of Sharia Services Remains Limited

Even though most respondents showed a basic understanding of Islamic finance principles, the use of sharia services in real practice is still pretty limited. Out of 15 respondents interviewed, only four actively used sharia banking products, either murabahah financing for business capital or wadiah savings as a savings instrument. This limitation is not solely due to a lack of interest. Still, it is also influenced by factors such as the uneven accessibility of sharia financial institutions in rural areas, limited understanding of the variety of sharia products, and the perception that procedures and requirements in sharia banking are more complex than conventional banking. This condition reflects a gap between religious awareness that encourages a preference for sharia-based services and the practical reality that makes most MSME players still dependent on the conventional financial system.

In daily practice, the most widely known and applied sharia contracts are:

a. Murabahah
73% of informants use it mainly to purchase merchandise or business assets. One informant said, "I bought a motorcycle for my business through a sharia bank, using the murabahah system. The price is clear from the start, there is no interest" (online motorcycle taxi informant).

b. Mudharabah
Implemented by around 40% of informants, generally in the form of partnerships with fellow business actors or local investors, as explained by one MSME actor, "I collaborate with a friend, he provides the capital, I run the business. Profits are divided according to the initial agreement" (Informant from a food stall).

c. Qardh Hasan
Interest-free loans between business operators are still practiced, though they are limited to 27% of informants. These loans are typically based on trust and social solidarity.

d. Professional Zakat
Almost all informants (87%) admitted to consistently paying professional zakat from their business profits, which is considered a religious obligation and a means of maintaining the blessings of their livelihood. These findings indicate that although the formal utilization of sharia financial products remains low, sharia values and practices are still internalized in the economic activities of MSME actors through formal contracts and sharing traditions based on the principles of justice and solidarity.

Accessibility Barriers

Many MSME players in rural areas admit to facing various obstacles in accessing Islamic financial services, prompting them to more frequently use conventional financial institutions or local cooperatives that are more accessible. One of the main obstacles is accessibility, as the distance to Islamic financial institution branches is relatively far, making them reluctant to conduct routine transactions. Additionally, administrative procedures perceived as more complex and requiring numerous requirements also explain why most business owners prefer conventional alternatives, which are considered more practical. Another challenge is the lack of awareness and education about Islamic financial products, resulting in limited understanding beyond basic concepts and a lack of knowledge of the variations of instruments that could be utilized. Furthermore, transaction costs that are relatively higher compared to conventional services further reinforce the perception that Islamic financial services are less practical. These factors collectively indicate a gap between the religious idealism driving the preference for the Islamic system and the technical realities that make its implementation still challenging for SMEs in rural areas.

Practicality is More Important than belief.

The findings show that practicality is still more important than religious belief in determining the choice of financial services for MSME players in practice. Although most respondents believe Islamic finance aligns more with sharia principles and provides spiritual peace, this has not been fully realized in actual practice. For them, business needs that demand speed and flexibility make aspects such as ease of access to financial institutions, simple administrative requirements, and quick fund disbursement processes the primary considerations. In other words, the religious idealism driving preferences for the Sharia system often must contend with pragmatic realities, where time constraints, costs, and resource limitations compel them to choose the most accessible financial services, even if they originate from conventional institutions.

The Phenomenological Experience of MSMEs

In the perspective of the phenomenological approach, the experiences of MSME actors with Islamic finance practices not only demonstrate rational choices in managing their businesses, but also reflect a much more complex dynamic between religious idealism rooted in a deep belief in upholding Islamic teachings in every aspect of life, including economic activities, with practical realities shaped by limitations in knowledge, accessibility, and the daily economic demands that often force them to make pragmatic decisions to ensure the sustainability of their businesses and meet family needs.

a. For some business owners, using Islamic financial services provides spiritual peace of mind because they believe it aligns with Islamic teachings. They feel more comfortable and confident that their economic activities are profit-oriented and have religious value. However, limitations in knowledge and access to Islamic financial products prevent this peace of mind from being fully realized in all aspects of their economic practices.
b. A significant dilemma arose among the informants. On the one hand, they strongly desire to consistently apply Islamic principles in their financial activities. However, limited economic conditions and minimal access to Islamic financial institutions in rural areas force some MSME players to remain dependent on conventional financial institutions. This creates ambivalence between urgent economic needs and religious awareness that demands full compliance with sharia.
c. There are also positive experiences directly felt by SME actors who have used Islamic financial services, particularly regarding the profit-sharing system. They consider this mechanism fairer than the fixed interest rates imposed by conventional financial institutions. With the profit-sharing system, payment burdens adjust according to business performance, so they feel less pressured when business results decline and are more motivated to increase productivity when the company grows. This sense of fairness and partnership in transactions reinforces the belief that Islamic finance is not merely an alternative but a solution that aligns more closely with the values of rural communities, which prioritize justice, solidarity, and blessings.

DISCUSSION

This research confirms a clear gap between ideal perceptions and actual practices in applying Islamic finance among MSME players. Most respondents generally showed positive perceptions of sharia principles, mainly because they are considered fairer, free of usury, and in line with the religious values they adhere to. However, when it comes to implementation, the application of Islamic financial services remains limited and is often hindered by external factors. This can be explained through the Theory of Planned Behavior (TPB), which emphasizes that intention does play an essential role in driving behavior. Still, intention does not always automatically materialize without support from situational factors such as adequate regulations, easily accessible service infrastructure, and a supportive social environment. In this context, a study by Norizan et al., (2025) found that attitude, subjective norm, and perceived behavioral control have a significant relationship with financial well-being in Islamic social finance, indicating a connection between perception and practice through the TPB pathway.

The results of the study indicate that the level of understanding of MSME actors regarding Islamic finance is still relatively low, with most informants only having a basic knowledge of concepts such as the prohibition of usury or interest, without a more comprehensive understanding of other sharia principles, such as profit-sharing systems, various contracts, or the prohibition of gharar and maisir. This limited understanding also has implications for the low utilization of Islamic financial products that could support their businesses' development. Most MSME players still have limitations in understanding more complex financial management practices, which could potentially become an obstacle in optimally utilizing Islamic financial products. This condition shows that their ability to manage business finances is often simple and not integrated with more advanced financial principles. In the Indonesian context, financial literacy is the primary foundation for creating a healthy and sustainable MSME financial management system (Dwyanti, 2024; Putri & Husna, 2024). Therefore, more intensive efforts are needed through educational programs and mentoring to ensure that SME operators not only understand the basic concepts but can also apply Islamic financial instruments in their daily business practices.

The fact that only a small percentage of respondents actually use Islamic financial products reflects a significant gap between ideal perceptions and actual practices. Within a phenomenological framework, this gap can be understood as a form of internal conflict experienced by MSME actors, namely the tension between their religious values and the demands of their daily economic needs. On one hand, they aspire to the blessings, peace of mind, and justice believed to be inherent in the Islamic financial system. However, on the other hand, the realities on the ground force them to rely more heavily on conventional financial services, particularly due to practical factors such as the ease of procedures, the proximity of financial institutions, and the speed of fund disbursement, which better align with the urgent needs of their businesses. This situation highlights that while religious awareness has shaped the intention to transition to the Islamic system, structural and technical limitations remain the primary barriers to achieving practices consistent with Islamic values.

Halal has proven to be an essential factor in MSMEs' perception of Islamic finance. Many MSME players, especially those engaged in the halal sector, emphasize that business success is determined by the halal nature of the product and the source of financing used. Several studies indicate that while halal SMEs understand Sharia principles well, the penetration rate of Sharia financing remains relatively low due to the lack of connectivity between the halal sector and Sharia financial institutions (Jaffar & Musa, 2014). Religious factors have proven to be the primary driver in shaping SMEs' positive attitudes toward Islamic financing, where religious obligations are the strongest determinant in the intention to adopt sharia financial services (Jaffar & Musa, 2014). Additionally, research in Malaysia indicates that knowledge and acceptance of Islamic finance positively correlate with the implementation of Sharia financial management in the business practices of halal SMEs, reinforcing the need for comprehensive integration between halal production and Sharia financing (Awang et al., 2020).

The potential for developing Islamic finance in Indonesia is enormous, particularly because the majority of the population is Muslim and the MSME sector dominates the economy, especially in rural areas. This makes MSMEs a potential market for Islamic financial products and services that align with the community's religious and social values. The principles of Islamic finance, which emphasize justice, transparency, and cooperation, align with traditional rural community values such as mutual aid and honesty, making them more easily accepted by local communities (Fianto & Gan, 2017). Moreover, the development of Islamic financial technology (fintech) has opened up broader access for rural SMEs that were previously difficult to reach by conventional financial services, thereby enhancing financial inclusion and accelerating the adoption of Islamic financial services (Lautania et al., 2024). Government support is also crucial, as various policies and programs aimed at developing the Islamic financial sector and empowering SMEs provide a positive momentum to strengthen this ecosystem.

CONCLUSION

This study thoroughly examines the perceptions and practices of micro, small, and medium enterprises (MSMEs) in rural areas regarding Islamic finance using a phenomenological qualitative approach. The study results reveal a clear gap between ideal views and actual practices in implementing Islamic finance. Most respondents positively perceive Sharia principles, which are considered fairer, interest-free, and aligned with the religious values they hold dear. However, implementing Islamic financial services still faces various obstacles, ranging from limited access to Sharia-compliant financial institutions and complex administrative procedures to a lack of in-depth understanding of the variety of Sharia-compliant products available. This situation indicates that while religious awareness has driven the intention to use Sharia-based financial systems, structural and technical factors remain the primary barriers to achieving financial practices fully aligned with Islamic principles.

Moreover, this finding highlights the significant potential for the development of Islamic finance in Indonesia, considering that the majority of the population is Muslim and MSMEs play a dominant role in the economy, especially in rural areas. The principles of Islamic finance, which emphasize fairness, transparency, and cooperation, align with the social values of rural communities, such as mutual assistance and solidarity, making them relatively easier to accept. Furthermore, the development of Islamic financial technology (fintech) opens new opportunities for rural MSMEs to access financial services that were previously difficult to reach, thereby promoting financial inclusion and accelerating the adoption of Islamic services. Additionally, government support through policies, regulations, and MSMEs empowerment programs, along with strengthening the Islamic finance sector, are key factors in reinforcing this ecosystem. Through the synergy of religious values, technological innovation, and policy interventions, Islamic finance has the potential to grow into a crucial pillar in strengthening the resilience and sustainability of MSMEs in Indonesia.

REFFERENCE

Abdeldayem, M., & Aldulaimi, S. (2023). Developing an Islamic Crowdfunding Model: A New Innovative Mechanism to Finance SMEs in the Middle East. *International Journal of Organizational Analysis*, *31*(6), 2623– 2644. https://doi.org/10.1108/IJOA-02-2022-3159

Ajzen, I. (1991). The Theory of Planned Behavior. *Organizational Behavior and Human Decision Processes*, *50*(2), 179– 211. https://doi.org/10.1016/0749-5978(91)90020-T

Akpan, I. J., Soopramanien, D., & Kwak, D.-H. (Austin). (2021). Cutting-edge Technologies for Small Business and Innovation in the Era of COVID-19 Global Health Pandemic. *Journal of Small Business & Entrepreneurship*, *33*(6), 607– 617. https://doi.org/10.1080/08276331.2020.1799294

Antonio, M. S. (2001). *Bank Syariah: Dari Teori ke Praktik*. Gema Insani. https://books.google.co.id/books?id=r3yFiZMvgdAC

Awang, M. D., Muhammad, J., Noor, M. N. A. M., Abdullah, A., Abdullah, A. A., Abdullah, N., & Abai, D. S. A. (2020). Knowledge, Acceptance and Application of Islamic Financial Management among Small and Medium Enterprises (SMEs) Halal Entrepreneurs in Peninsular of Malaysia. *KnE Social Sciences*. https://doi.org/10.18502/kss.v4i9.7327

Ayub, M. (2007). *Understanding Islamic Finance*. John Wiley & Sons Ltd. https://www.ajindex.com/dosyalar/kitap/acarindex-1424384539.pdf

Balushi, Y. Al, Locke, S., & Boulanouar, Z. (2019). Determinants of the Decision to Adopt Islamic Finance: Evidence from Oman. *ISRA International Journal of Islamic Finance*, *11*(1), 6– 26. https://doi.org/10.1108/IJIF-02-2018-0020

Dwyanti, D. (2024). The Importance of Financial Literacy in Financial Management in Micro, Small and Medium Enterprises (MSMEs). *Journal of Applied Management and Business*, *5*(1), 1– 6. https://doi.org/10.37802/jamb.v5i1.661

Fianto, B. A., & Gan, C. (2017). Islamic Microfinance in Indonesia. In *Microfinance in Asia* (pp. 227–270). WORLD SCIENTIFIC. https://doi.org/10.1142/9789813147959_0007

Jaffar, M. A., & Musa, R. (2014). Determinants of Attitude towards Islamic Financing among Halal-certified Micro and SMEs: A Preliminary Investigation. *Procedia - Social and Behavioral Sciences*, *130*, 135– 144. https://doi.org/10.1016/j.sbspro.2014.04.017

Lautania, M. F., Mutia, E., Evayani, & Dinaroe. (2024). *Islamic Fintech in Indonesia: Opportunities and Challenges for Growth and Innovation* (pp. 283– 291). https://doi.org/10.1007/978-3-031-55911-2_27

Maksum, I. R., Rahayu, A. Y. S., & Kusumawardhani, D. (2020). A Social Enterprise Approach to Empowering Micro, Small and Medium Enterprises (SMEs) in Indonesia. *Journal of Open Innovation: Technology, Market, and Complexity*, *6*(3), 50. https://doi.org/10.3390/joitmc6030050

Manzoor, F., Wei, L., & Sahito, N. (2021). The Role of SMEs in Rural Development: Access of SMEs to Finance as a Mediator. *Plos One*, *16*(3), e0247598. https://doi.org/10.1371/journal.pone.0247598

Mengistu, A. T., & Panizzolo, R. (2023). Tailoring Sustainability Indicators to Small and Medium Enterprises for Measuring Industrial Sustainability Performance. *Measuring Business Excellence*, *27*(1), 54–70. https://doi.org/10.1108/MBE-10-2021-0126

Nath, H. (2024). Role Micro, Small and Medium Enterprises (MSMEs) in Indian Economy. *ShodhKosh: Journal of Visual and Performing Arts*, *5*(1). https://doi.org/10.29121/shodhkosh.v5.i1.2024.2784

Norizan, S. N. B., Abu Bakar, N. B., Iqbal, M. S., & Idris, I. B. M. (2025). Examining Financial Well-being among Students: Islamic Social Finance and Theory of Planned Behavior Approach. *Review of Islamic Social Finance and Entrepreneurship*, 1–16. https://doi.org/10.20885/RISFE.vol4.iss1.art1

Panakaje, N., Parvin, S. M. R., Bhagwath, A. A., Siddiq, A., Irfana, S., & A, Y. (2025). Measuring Socio-

Economic Development of Rural Households: Scale Development. *Cogent Social Sciences*, *11*(1). https://doi.org/10.1080/23311886.2025.2473766

Perez-Trujillo, M., & Lacalle-Calderon, M. (2020). The Impact of Knowledge Diffusion on Economic Growth Across Countries. *World Development*, *132*, 104995. https://doi.org/10.1016/j.worlddev.2020.104995

Pitchay, A. B. A., Thaker, M. A. B. T., Azhar, Z., Mydin, A. A., & Thaker, H. B. M. T. (2019). Factors Persuade Individuals' Behavioral Intention to Opt for Islamic Bank Services. *Journal of Islamic Marketing*, *11*(1), 234–250. https://doi.org/10.1108/JIMA-02-2018-0029

Putri, A. R., & Husna, F. K. (2024). Financial Management Analysis of Culinary Micro, Small, and Medium Enterprises (MSMEs). *Journal of Economics Research and Policy Studies*, *4*(1), 68–78. https://doi.org/10.53088/jerps.v4i1.858

Raspati, F. A., & Kadiyono, A. L. (2023). Micro, Small and Medium Enterprises (MSMEs): Women's Empowerment for Women Entrepreneurs. *Sawwa: Jurnal Studi Gender*, *18*(1), 25–48. https://doi.org/10.21580/sa.v18i1.14430

Salsabillah, W., Hafizzallutfi, Uut Tarissyaa, Nur Azizah, Thia Fathona, & Muhammad Raihan. (2023). The Role of Micro, Small, and Medium Enterprises (MSMEs) in Supporting the Indonesia Economy. *Indonesian Journal of Multidisciplinary Sciences (IJoMS)*, *2*(2), 255–263. https://doi.org/10.59066/ijoms.v2i2.339

Sularsih, H., & Nasir, A. (2021). Strategi UMKM dalam Meningkatkan Pendapatan Dimasa Pandemi Covid-19 Guna Mempertahankan Kelangsungan Usaha di Era Revolusi Industri 4.0 (Studi pada UMKM Makanan dan Minuman di Kabupaten Pasuruan). *Jurnal Paradigma Ekonomika*, *16*(4), 763–772. https://doi.org/10.22437/jpe.v16i4.14770

Swain, R. B., & Ranganathan, S. (2021). Modeling Interlinkages between Sustainable Development Goals Using Network Analysis. *World Development*, *138*, 105136. https://doi.org/10.1016/j.worlddev.2020.105136

Zreik, M., & Haron, N. F. (2025). The Impact of Social Financial Grants on Poverty Alleviation in Rural Indonesia: A Demographic and Econometric Analysis. *Asian Social Work and Policy Review*, *19*(2). https://doi.org/10.1111/aswp.70011